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State Auditor Vaudt Reviews Governor's Fiscal Year 2009 Budget
While making progress, challenges loom for Fiscal Year 2010

(Des Moines, Iowa) – Continuing in his role as the “Taxpayers’ Watchdog” and his duty to report directly to the people of Iowa on the condition of the State’s finances, State Auditor David A. Vaudt has completed his review of the Governor’s proposed Fiscal Year 2009 budget.

While the Governor’s Fiscal Year 2009 budget proposal makes significant progress in enhancing clarity, reducing the spending gap, and lowering spending growth, it sets Iowa up for some difficult challenges in the following fiscal year. Some of the reasons Auditor Vaudt cited for this include:

Iowa’s “Charge Cards” are Maxed Out

The Governor’s budget “maxes out” Iowa’s charge cards – the funds used for the past several years to balance the budget. These funds include the Senior Living Trust Fund, various tobacco related funds, and the Property Tax Credit Fund. “The depletion of these funds in Fiscal Year 2009 creates a \$193 million hole for Fiscal Year 2010,” commented Auditor Vaudt. “The question taxpayers should be asking is—how does the Governor propose to fill that hole?”

Bonding Leaves Future Generations Paying for Current Year Operating Expenditures

One-time bond proceeds of \$67 million are used to balance the Fiscal Year 2009 operating budget, and taxpayers will pay for those services for decades to come. Auditor Vaudt stressed, “This is contrary to good budgeting principles because this practice leaves future generations to pay for current year operating expenditures.”

Spending Continues to Exceed Revenue

Auditor Vaudt noted planned expenditure growth of 16% over a two-year period (Fiscal Year 2008 and Fiscal Year 2009) still outpaces anticipated ongoing revenue growth of 12% over the same time period. Auditor Vaudt added, “Considering 80% of that two-year revenue growth comes from tax and fee increases, it’s obvious the trends in expenditure growth are unsustainable through economic growth alone. To spend at such a torrid pace, we must increase taxes and fees at a torrid pace. That, in turn, could adversely impact economic growth in our state.”

Rainy Day Funds Provide False Sense of Security

“With \$600 million sitting in the “Rainy Day” funds, it’s easy to get a false sense of security,” Auditor Vaudt cautioned. Considering the \$361 million spending gap built into the Fiscal Year 2010 budget, a substantial revenue shortfall could wipe out the “Rainy Day” funds in just one year, Auditor Vaudt warned. “With a looming threat of recession, such a scenario is entirely possible.”

Infrastructure Funds Diverted for General Fund Expenditures

The Governor’s budget proposal makes a statutory reallocation of \$90 million from long-term infrastructure spending to fund General Fund services. “As last year’s bridge collapse in Minnesota underscored, states across the country are facing the need for increased infrastructure spending,” commented Auditor Vaudt. “It makes no sense to borrow money for a prison as the Governor’s budget proposes to do, while at the same time divert a large infrastructure revenue source that could pay for a substantial portion of such a project without incurring debt in the first place.”

Short-Term Focus Continues

“Longer-term planning will allow us to assess how today’s decisions will impact tomorrow’s budgets,” said Auditor Vaudt. “The Governor’s budget proposal calls for a 5.7% increase in spending next year, but it also sets Iowa up with at least a 5.7% spending gap, \$361 million, the following year. It’s appropriate to ask the Governor how he plans to bridge that gap. Will it be through tax and fee increases, or will he find areas to reduce spending? Iowans want to know where the Governor is leading them.” Auditor Vaudt also refuted the notion planning 2 years ahead is too difficult, noting the accuracy of his prediction last year the Legislature would increase expenditures at least 5.5% as a consequence of the commitments made in the 2007 session. The Governor’s budget proposal calls for a 5.7% increase in spending.

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**Auditor of State
David A. Vaudt**

**Comments on
Governor Culver's & Lt. Governor Judge's
Fiscal Year 2009 Proposed Budget**

**February 12, 2008
Press Briefing**

State of Iowa FY09 General Fund Budget

Remarks today will focus on five areas:

- Progress made in key budget elements for FY09
- Other FY09 budget facts Iowans need to understand
- A two-year snapshot - FY08 & FY09
- Looking to FY10 - what does the picture look like?
- Summary take aways

State of Iowa

FY09 General Fund Budget

Progress - Key Budget Elements

(\$ in Millions)

Enhanced Clarity - \$180.9 million reduction in expenditures shifted to other special funds and accounts with minimal under-funded costs.

	<u>FY09 Governor's Proposal</u>	<u>FY08 Adopted Budget</u>
Expenditures as presented	\$6,399.6	\$5,862.9 (A)
Additional expenditures:		
Non-General Fund resources	241.2	422.1
Under-funded costs	<u>13.5</u>	<u>12.6</u>
True total expenditures	<u><u>\$6,654.3</u></u>	<u><u>\$6,297.6</u></u>

(A) Adjusted for \$6.6 million of FY09 Workforce Development withholding and Childcare credit shifts to General Fund.

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FY09 General Fund Budget

Progress - Key Budget Elements

(\$ in Millions)

Reduced Spending Gap - \$189.1 million reduction in the amount by which true total expenditures exceed total revenues (as adjusted for all resources).

	<u>FY09 Governor's Proposal</u>	<u>FY08 Adopted Budget</u>
Total revenues	<u>\$6,548.0</u>	<u>\$5,989.8</u>
Revenues available (A)	\$6,475.3	\$5,922.9
True total expenditures	<u>6,654.3</u>	<u>6,291.0</u>
Spending gap	<u>\$ (179.0)</u>	<u>\$ (368.1)</u>

(A) Reflects 99% expenditure limitation reduction (FY09-\$72.7 million, FY08-\$66.9 million)

**State of Iowa
FY09 General Fund Budget
Progress - Key Budget Elements
(\$ in Millions)**

Lowered Spending Growth - 5.7% increase in FY09 spending compared to 9.7% increase in FY08.

True total expenditures:

FY07	<u><u>\$5,739.8</u></u>		
		<u><u>\$557.8</u></u>	<u><u>9.7%</u></u>
FY08	<u><u>\$6,297.6</u></u>		
		<u><u>\$356.7</u></u>	<u><u>5.7%</u></u>
FY09	<u><u>\$6,654.3</u></u>		

State of Iowa FY09 General Fund Budget "The Rest of the Story"

Fact 1: Iowa's "charge cards" (except for "Rainy Day" funds) are essentially "maxed out" under this budget proposal.

- Senior Living Trust Fund (\$74.6 million)
- Tobacco Related Funds (\$36.3 million):
 - Endowment for Iowa's Health Account
 - Restricted Capital Fund
 - Healthy Iowans Tobacco Trust Fund
 - Endowment for Iowa's Health Restricted Capitals Fund
- Property Tax Credit Fund (\$81.8 million)

Impact: A total of \$192.7 million of resources used in FY09 "disappear" in FY10. However, the expenditures are ongoing. Yes, even the Senior Living Trust Fund we have been "repaying" will be essentially depleted.

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FY09 General Fund Budget
"The Rest of the Story"

Fact 2: This budget proposal uses bonding to pay current expenditures. Iowa should never use this financial maneuver!

Impact: Another \$67.0 million of resources "disappear" in FY10 — but we will be paying for these FY09 services for decades to come!

State of Iowa FY09 General Fund Budget "The Rest of the Story"

Fact 3: This budget proposal makes a statutory reallocation of \$90 million of gaming revenues from long-term infrastructure spending to current General Fund service spending.

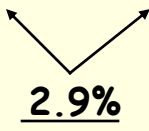
Impact: With the Governor's proposal for significant FY09 corrections infrastructure spending, coupled with all the concern about Iowa's roads and bridges infrastructure needs—it begs the question—Is now the time to redirect infrastructure monies to General Fund spending?

State of Iowa

FY09 General Fund Budget

A Two-year Snapshot - Revenue Increases (\$ in Millions)

Tax and fee increases account for 80.0% of the \$835.5 million revenue growth in the FY08 and FY09 two-year period.

	<u>Total Revenues</u>	<u>Newly Enacted Revenues (A)</u>	<u>% Newly Enacted Revenues</u>
FY08 growth	\$342.0	\$181.9	<u>53.2%</u>
FY09 growth	<u>493.5</u>	<u>486.2</u>	<u>98.5%</u>
Total revenue growth	835.5	668.1	<u>80.0%</u>
Less one-time revenues	<u>(131.6)</u>	<u>(131.6)</u>	
Ongoing revenues growth	<u>\$703.9</u>	<u>\$536.5</u>	
Two-year % increase (B)	<u>12.3%</u>	<u>9.4%</u>	
			<u>2.9%</u>

(A) 2007 enacted and 2008 proposed changes

(B) Based upon FY07 base revenues (\$5,712.5)

State of Iowa

FY09 General Fund Budget

A Two-Year Snapshot - Spending Increases

(\$ in Millions)

On the other hand, spending over the same two-year period would increase \$914.5 million, or 8.0% average annual growth—funded primarily by increased taxes and fees.

Spending growth:

FY08 true total expenditures	\$557.8
FY09 true total expenditures	<u>356.7</u>
Total spending growth	<u>\$914.5</u>
Two-year % increase (A)	<u>15.9%</u>

(A) Based upon FY07 expenditures (\$5,739.8).

State of Iowa FY09 General Fund Budget The FY10 Outlook (\$ in Millions)

Even with significant tax and fee increases in FY08 and FY09, spending increases continue to outpace revenues available.

FY09 revenues		\$ 6,548.0
Less: FY09 one-time revenues	\$ (103.3)	
FY10 impacts of enacted revenue reductions and tax credit increases	<u>(87.5)</u>	<u>(190.8)</u>
FY09 <u>ongoing</u> revenues		<u>\$ 6,357.2</u>
FY09 <u>ongoing</u> revenues available (A)		<u>\$ 6,293.6</u>
FY09 true total expenditures		<u>6,654.3</u>
Spending gap for FY10 before revenue and spending increases		<u>\$ (360.7)</u>
FY10 revenue growth needed just to fill the existing spending gap		<u><u>5.7%</u></u>

(A) Reflects 99% expenditure limitation reduction (\$63.6)

State of Iowa FY09 General Fund Budget The FY10 Outlook (\$ in Millions)

In addition, the use of one-time revenues further magnifies the problem, contributing to a \$360.7 million FY10 spending gap before revenue and spending increases are considered.

FY09 revenues		\$ 6,548.0
Less: FY09 one-time revenues	\$ (103.3)	
FY10 impacts of enacted revenue reductions and tax credit increases	<u>(87.5)</u>	<u>(190.8)</u>
FY09 <u>ongoing</u> revenues		<u>\$ 6,357.2</u>
FY09 <u>ongoing</u> revenues available (A)		<u>\$ 6,293.6</u>
FY09 true total expenditures		<u>6,654.3</u>
Spending gap for FY10 before revenue and spending increases		<u>\$ (360.7)</u>
FY10 revenue growth needed just to fill the existing spending gap		<u><u>5.7%</u></u>

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State of Iowa FY09 General Fund Budget Bottom Line Take Aways

- While FY09 budget proposal makes significant progress in enhancing clarity, reducing the spending gap, and lowering spending growth, it sets Iowa up for a difficult FY10.
- The budget “maxes out” Iowa's charge cards—the funds used for the past several years to balance the budget (Senior Living Trust Fund, Tobacco-related funds, Property Tax Credit Fund). That's a \$193 million impact to FY10.

State of Iowa FY09 General Fund Budget Bottom Line Take Aways

- One-time bond proceeds of \$67 million are used to balance the FY09 operating budget, and we will pay for those FY09 services for decades to come! This is contrary to good budgeting principles.
- Even with tax and fee increases providing 80% of revenue growth in the FY08 and FY09 two-year period, expenditure growth of 16% still outpaces ongoing revenue growth of 12%. This is unsustainable.
- With a \$361 million spending gap built into FY10, a substantial revenue shortfall could wipe out the "Rainy Day" funds in one year—even without a spending increase.

State of Iowa FY09 General Fund Budget Bottom Line Take Aways

- Oddly, the proposed reallocation of \$90 million from infrastructure spending to General Fund spending comes during a time of rising infrastructure needs.
- Even with significant tax and fee increases, under Iowa's short-term focus, spending continues to exceed available revenues. A longer-term financial plan is sorely needed to map our financial future—this one-year focus, “kick the can down the road” approach, has to stop.